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No. 82-342

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

PHILKO AVIATION, INC.,

Petitioner,

vs.

MAURICE SHACKET and SYLVIA SHACKET,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

REPLY BRIEF FOR PETITIONER

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PETITION FOR CERTIORARI FILED AUGUST 20, 1982
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QUESTIONS PRESENTED

By enacting Section 1403 of the Federal Aviation Act, 49 U.S.C. Section 1403 (1981), requiring the recordation of conveyances affecting aircraft, did Congress preempt state law insofar as state law would permit the conveyance of title to aircraft by transfer of possession alone, without FAA recording?

Philko Aviation, Inc., the Petitioner herein, is a wholly owned subsidiary of McArdle, Ltd., a Delaware Corporation. Philko Aviation, Inc. has no subsidiaries. McArdle, Ltd. has the following wholly owned subsidiaries in addition to Philko Aviation, Inc.: Airport Farms, Inc.; American Lodging Corp.; Big Flamingo II, Inc.; Bonhomme Richard, Ltd.; Burr Hill Country Club Inc.; Burr Hill Properties, Ltd.; Forty-Six East Oak, Ltd.; Pheasant Run, Inc.; Rockton Productions, Inc.; Smith Road Properties, Inc.; Spanish Lakes, Inc. and Wilson World Travel, Inc.

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ARGUMENT

I.

SHACKET'S FAILURE TO RECORD WITH THE FAA WAS CAUSED BY HIS OWN FAILURE TO OBTAIN ORIGINAL BILLS OF SALE AND FILE THEM WITH THE FAA.

The issue in this proceeding is whether the recording provisions of Section 503, 49 U.S.C. §1403 (1981) preempt any state law which permits the conveyance of title to aircraft, valid as to third parties without notice, by

transfer of physical possession alone without FAA recording. Shacket's restatement of the Question Presented attempts to shift the Court's focus away from the true issues by alluding to his claimed status as a bona fide purchaser and by blaming the seller, Smith, Inc., for the failure to record. Shacket's failure to record, however, was caused by his own failure to insist upon and obtain the original bills of sale for the new Piper Navajo aircraft and failure to forward them to the FAA. In the concluding portion of his brief (Respondent's Brief p. 37) Shacket claims that his recording would not have prevented Philko's loss because of the short time period between the two transactions. This argument overlooks the obvious fact that Smith, Inc. would not have had original bills of sale to give Philko if Shacket had demanded them. Shacket concedes that Congress intended to enact a central recording system. (Respondent's Brief p. 22) A recording system requires that parties conduct their dealings with respect to aircraft by delivering instruments which can be recorded. Shacket never received a recordable instrument from Smith, Inc.

II.

THE LEGISLATIVE HISTORY OF SECTIONS 503 AND 506, INCLUDING THE SUBCOMMITTEE HEARINGS, DEMONSTRATES THAT THE FAILURE TO RECORD NULLIFIES AN INTEREST IN AIRCRAFT WITH RESPECT TO THIRD PARTIES WITHOUT NOTICE.

Petitioner Philko has previously discussed Senate Report No. 1060, 88th Cong., 2d Sess. 2 (1964) which reflects Congress' intent to continue the recording system for aircraft while providing a rule for choice of law on the substantive validity of *recorded instruments*. (Petitioner's Brief pp. 21-23) Respondent argues that the Sub-

committee hearings prior to the enactment of Section 506 reflect the view that the failure to record should have no negative impact upon priorities or other substantive rights of parties dealing with aircraft. This is not an accurate reading of the plain language of Sections 503 and 506 or the statements at the subcommittee hearings. Without doubt the drafters of Section 506 understood that a conveyance or encumbrance could not have substantive legal effect as against third parties without notice thereof unless such conveyance or encumbrance was filed for recordation with the FAA. The sponsors of Section 506 never intended to change this precept. Dee Martin Calligar, one of the principal draftsmen of Section 506, testified as follows:

* * *

> MR. CALLIGAR: The point there, Congressman Springer, is that we provide that one State's laws will determine the validity of the instrument between the parties *and that if the instrument is recorded with FAA* it will be deemed valid against all persons, all subsequent encumbrances, creditors, or purchasers.
>
> The scheme of things in this bill follows somewhat the scheme of things in the Federal Aviation Act as it is now written. Section 503(d) of the act provides that if an instrument is recorded with the Federal Aviation Agency it is valid and binding upon all persons in the United States.
>
> The provision you quote says the same thing, only it goes to the point of validity.
>
> * * *
>
> MR. SPRINGER: This is the point I am trying to raise. Suppose that you in New York take a mortgage on an airplane in Illinois, Ozark was one that you were pretty close to a minute ago which travels

across my district. Suppose that someone wants to buy an airplane from Ozark, we will say, under some circumstances.

How are they going to find out? Are they going to have to search through all 50 states to find if there is an encumbrance against that plane before they buy it?

MR. CALLIGAR: No. *The Federal Aviation Act itself provides for a recording system as to all encumbrances affecting title to aircraft. To be valid as against other persons, the instrument must be filed with the Federal Aviation Agency. That is the only place one need look to determine if there is any encumbrance on the aircraft. That is presently in the act, sir.*

MR. SPRINGER: All right. *In other words, it has to be filed with that Agency and you would have to file yourself with that Agency?*

MR. CALLIGAR: Yes.

MR. SPRINGER: *Is this so clear by the Federal Aviation Act that if you do file an encumbrance that a purchaser in good faith, all he has to do is check with the Federal Aviation Agency?*

MR. CALLIGAR: *Yes, it is so clear. It has been since the act was adopted.*

MR. SPRINGER: *No question about that.*

MR. CALLIGAR: *No question in my mind.*

MR. SPRINGER: Is there any providing for a recording by the FAA or is that instrument merely on file with them?

MR. CALLIGAR: Sir?

MR. SPRINGER: I am talking about the present law.

MR. CALLIGAR: The present law requires that such an instrument must be filed for record with the FAA.

MR. SPRINGER: And with them only?

MR. CALLIGAR: With them only.

MR. SPRINGER: It does not have to be filed with the district recorder?

MR. CALLIGAR: No. *The Federal recording provision preempts the law on that point, State recording laws to the contrary notwithstanding.*

MR. SPRINGER: Then they do not have to record that, we will say, in St. Louis or Champaign County, Ill.?

MR. CALLIGAR: They do not.

MR. SPRINGER: All right. There is no doubt about the law on that question. Now, what you are seeking then is to apply to the contract action itself the law of the State of New York for the most part, where most of these instruments would be executed?

MR. CALLIGAR: I dislike saying New York only.

MR. SPRINGER: We will say Chicago.

MR. CALLIGAR: All right.

MR. SPRINGER: All that you are seeking to do is apply the law of the State in which the instrument is delivered and recorded; is that correct?

MR. CALLIGAR: *In which the instrument is delivered, assuming that it is then recorded with the Federal Aviation Agency as the Federal Aviation Act requires. That step must be taken.*

A Bill to Amend Section 503 of the Federal Aviation Act: Hearing Before a Subcommittee of the Committee on Interstate and Foreign Commerce, 88 Cong., 1st Sess. 6-8 (1963) (Emphasis added).

Mr. Calligar emphatically stated that Section 506 was not intended to supplant the recording requirement of Section 503:

* * *

MR. SPRINGER: The point I am trying to get is this. We will say a creditor in Champaign County, Ill.—I do not know how he goes about this, but probably if he said, "I will give this as security or I do have it"—in order for him to file a suit and we will say to file a lien upon this man's aircraft would he have to look further than the courthouse in Urbana?

This is the point I am trying to get in my mind as to whether or not, even though you are not recording, you would have a preference by virtue of the fact we would be saying to you, because you have delivered this in the State of New York you comply in the State of New York, which undoubtedly would give you a lien without any question.

MR. CALLIGAR: No. *This bill does not go to the question of the applicability of State law as to the recorded status of the conveyance. In the case that you put, the first mortgage in Illinois would not be deemed notice to a second mortgagee or any other creditor because, as you put the case, the instrument was not recorded with the Federal Aviation Agency. The act requires that that be done.*

MR. SPRINGER: That is not quite the point. We will say that you do have a first mortgage. We will say this man then has a claim which he refused (sic) [reduced] to a judgment in the State of Illinois. He goes to the courthouse to see whether or not there is any lien against the aircraft. Then under the law of Illinois he would be entitled to levy upon the aircraft because there is no recordation in the courthouse in Urbana, but then under this you could raise a defense here to the State of New York law because this is where the instrument was delivered.

I am wondering whether we are going to get more complicated than we are. I realize you have complications here.

MR. CALLIGAR: I must disagree with the way you say it because currently the man would not be able to look to Illinois recording to see whether there was a mortgage on this aircraft. He must look to the Federal Aviation Agency recording branch in Oklahoma City because the Federal law requires that a mortgage to be deemed notice to the world must be recorded with the Federal Aviation Agency.

MR. SPRINGER: All aircraft?

MR. CALLIGAR: All aircraft.

Id. 13-14. (Emphasis added)

The preemptive effect of Section 503 was also recognized by James D. Hill, then General Counsel for the FAA, who testified in favor of Section 506 as follows:

* * *

MR. WILLIAMS: Mr. Hill, I wanted to ask you a question about this provision of H.R. 2522. On page 2 you make the statement that—

> Once an instrument is filed for recordation under the act, all persons are deemed to have constructive notice of its existence and its effect on the title of the aircraft involved.

MR. HILL: Yes.

MR. WILLIAMS: Let us take the hypothetical case of an aircraft which is financed in the State of New York by bank X. The bank in the State of New York records the instrument with the Federal Aviation Agency but does not record it with the State in the chattel mortgage records.

Subsequently, the man may have to have repairs or he may have to encumber his aircraft further so he goes to Y bank. Y bank takes a second mortgage and Y bank records this both in the State of New York and with the Federal Aviation Agency.

Under the laws of the State of New York, only the filing within the State of New York would constitute constructive notice.

In this case, would the second mortgage take priority over the first mortgage?

MR. HILL: No.

MR. WILLIAMS: Where constructive notice under the State law did not exist, but where under Federal law notice had been given.

MR. HILL: No, sir. *The effect of title 5 of the act is to preempt the field and to make State recording unnecessary. So that if X bank had recorded its first mortgage with the Federal Aviation Agency, it would be prior to Y mortgage even if it had not been recorded in New York. That is in subsection d.*

> Each conveyance or other instrument recorded under this system shall from the time of its filing for recordation be valid as to all persons without further or other recordation.
>
> MR. WILLIAMS: You think this effectively preempts State law?
>
> MR. HILL: Yes, sir; I think that is what it was intended to do.

Id. 21-22. (Emphasis added)

III.

PHILKO HAD NO NOTICE OF THE SHACKET TRANSACTION UNTIL AFTER IT FILED THE ORIGINAL BILLS OF SALE WITH THE FAA.

The district court below held that "Certainly there is no showing of fraud or a knowing interference with the Shackets' rights by Philko or McArdle." (Pet. App. 34a) There is no evidence in the record showing that Philko had any direct or indirect knowledge of Shackets' transaction until mid June of 1978, after the bills of sale had been filed. (R. E.M. Dep. 76-78, M.S.-2 Dep. 98-99) Given the highly mobile nature of aircraft, the absence of physical possession certainly is insufficient to put a party on notice of a possible adverse claim to the aircraft. By adopting the recording system Congress expressly sanctioned the use of documents rather than possession as a means of effecting conveyances of aircraft. Shacket claims to be a buyer in the ordinary course of business. This requires that he act in good faith and without knowledge that the sale to him was in violation of the ownership rights or security interest of a third party in the goods. Ill. Rev. Stat. Ch. 26, §1-201(9) (1961) It is uncontroverted that Shacket accepted xerox copies of the original bills of sale from Piper Aircraft to North States Aviation, North States Aviation to Clark Aviation and

Clark Aviation to Smith, Inc., and a purchaser's carbon copy of the bill of sale from Smith, Inc. to himself. (R. M.S.-2 Dep. 53-56) Although these copies reflected that the originals had been completed, Shacket accepted Smith's excuse that the originals could not be delivered because his secretaries could not finish typing them. (R. J.H. Dep. 44-49) Shacket, not Philko, had notice of facts which should have provoked further inquiry of the circumstances. Moreover, section 1401, 49 U.S.C. §1401 (1981) requires that an owner register his aircraft before he flies it. The registration process requires that the owner show proof of ownership. 14 C.F.R. Sec. 47.31 (1980) Shacket's total disregard of the statutory registration and recording requirements, which he fully comprehended, vitiate any claim that he acted in good faith and without knowledge that the sale to him was in violation of the ownership rights or security interest of third parties. Even under State law Shacket's claim to title is flawed.

Respectfully submitted,

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